April 26, 2022

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington D.C. 20549

Re: Short Position and Short Activity Reporting by Institutional Investment Managers (File No. S7-08-22)

Dear Ms Countryman,

At the Standards Board for Alternative Investments (“SBAI”), we welcome the opportunity to submit comments on the U.S. Securities and Exchange Commission’s (“SEC”) Proposed Short Position and Short Activity Reporting by Institutional Investment Managers.¹

At the SBAI, we are an active alliance of over 150 asset managers and over 90 institutional investors dedicated to advancing responsible practices, partnership and knowledge. Our community includes asset managers with over $2 trillion in AUM and institutional investors responsible for over $4 trillion in assets, with a large proportion of them based in the U.S. or invested with investment managers in the U.S. We aim to improve industry outcomes through our Alternative Investment Standards², practical industry guidance³ and engagement with the global regulatory community⁴. Our mission is to bring asset managers and investors together to achieve new best practices and improve industry outcomes.

We support efforts to facilitate fair, orderly, and efficient markets, reduce systemic risk, and enable investors to make well informed investment decisions. SBAI is an Affiliate Member of the International Organization of Securities Commissions (IOSCO).

In our response to your request for input, we do not answer the specific questions raised, but highlight key positions and their rationale that we view as important when developing rules in the area of Short Position and Short Activity Reporting. This is due to the number of parallel requests for input published by the SEC during Q1 2022 and the limited time granted to respond to these requests, to properly assess the implications and craft a detailed response to the questions. Not answering the detailed questions should not be considered an endorsement of any or all the suggestions contained in that question.

We would ask the SEC to consider providing more time for responses to consultations of this nature going forward to aid with arriving at effective rules for the industry that support sound public policy.

¹ [https://www.sec.gov/rules/proposed/2022/34-94313.pdf](https://www.sec.gov/rules/proposed/2022/34-94313.pdf)
² [https://www.sbai.org/standards.html](https://www.sbai.org/standards.html)
³ [https://www.sbai.org/toolbox.html](https://www.sbai.org/toolbox.html)
⁴ [https://www.sbai.org/regulatory-engagement.html](https://www.sbai.org/regulatory-engagement.html)
Key Positions on the Proposal

1. We at the SBAI support regulatory authorities in their efforts to better understand the capital markets and assess potential systemic risks. In designing regulatory data collection efforts, it is important that they be proportionate and provide meaningful insight into the build-up of potential risk.

2. We agree with the SEC’s assessment of the important role of short selling:
   - as a tool to provide liquidity in response to unanticipated demand,
   - as a means for market participants to benefit from downward price movements, and
   - as a hedging tool for long positions.

As stated by the SEC, short selling improves price efficiency by providing information to the market. Short sellers act as market detectives, increase liquidity and can help mitigate market bubbles, to the benefit of all investors—not just to managers who implement investment strategies that involve short selling.5

3. We also agree with the SEC’s assessment of potential risks of short position disclosures, notably
   - reduction of “incentives to gather information about the marketplace and specific securities”,
   - “copycat trading”,
   - risk of “short squeezes”,

and that only aggregate, anonymized, and delayed public reporting of short positions mitigates these concerns. Avoiding these negative outcomes is of great importance to SBAI’s investor members as well as our manager members.

4. However, the new Proposed Form SHO data collection framework is not justified from a cost benefit perspective, given that it provides only very limited additional relevant insight compared to currently available data. Focus should instead lie on making enhancements to FINRA’s existing collection and dissemination of aggregate short interest data and making the existing CAT data collection related to short activity fit for purpose.
   - FINRA has already recently requested comment on “potential enhancements to its short sale reporting program” through Regulatory Notice 21-19 published on June 4, 2021.6 Such enhancements should be finalized and implemented prior to the SEC pursuing any rulemaking in this area.
   - Further, much of the additional relevant data that may be needed for regulatory supervision purposes is available in a timelier manner via the Consolidated Audit Trail (CAT), which will shortly be upgraded.
   - Implementing the Proposed Form SHO reporting infrastructure (as well as the monitoring of its accurate functioning) will incur significant cost on investment managers and ultimately end-investors.

Please see a more detailed rationale further below (Why the SHO Data Collection Framework is not justified from a cost benefit perspective).

5. The proposal suggests an improvement of the SEC’s “ability to respond to similar market events in the future” (p. 7). However, the newly proposed data framework will not provide timely insight for the SEC to act given that it is monthly data with 14 days delay after month end.

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• More importantly, it is unclear how the SEC will respond or intervene in “market events”, and how it establishes what constitutes a disorderly market and distinguishes it from a justified price correction.

• In fact, creating the expectation that regulators have the tools to intervene in markets to protect investors from price movements could have the opposite effect, by encouraging more risk taking by market actors who will rely on such regulatory intervention going forward.

Please see a more detailed rationale further below (Why well intended regulatory protection/intervention can increase risks and distress).

Why the SHO Data Collection Framework is not justified from a cost benefit perspective:

• The data collected via Proposed Form SHO and published in aggregate form pursuant to Proposed Rule 13f-2 will not promote “greater risk management among market participants”, and hence, not bolster “confidence in the markets” (p. 7) by providing greater transparency:
  o For risk management purposes, investors use information about aggregate short interest. Such (albeit currently not perfectly accurate) data is available via FINRA, the exchanges and data vendors – and notably, FINRA is already in the process of considering enhancements to its collection and dissemination of aggregate short interest data, including with respect to its timeliness and frequency.

• If the SEC’s concern is that CAT data is not accurate enough, focus should lie on enhancing the accuracy of this existing data.
  o As stated in the consultation, existing CAT reporting will be enhanced once the CAIS system becomes operational (footnote 246), enabling the retrieval of specific data from the CAT system (e.g. trade data for individual traders for regulators). It might therefore be advisable to wait for the availability of the better data, before a new, separate reporting framework is being established.

• Data collected via Proposed Form SHO will not provide a complete perspective on shorting activity, given that only data from substantial managers will be captured, and it does not account for other market participants (who are not managers), who might also engage in shorting activities.

• It is not clear why historic information related to the “lifecycle of a short sale” (p.8) beyond the aggregate current short interest is relevant to market participants.
  o Past trading activity is already reflected in the current market price, irrespective of whether short selling has occurred or not. The aggregate impact of short selling might have reduced the price, but this information is already reflected in the current market price.
  o The existing disclosure of aggregate short interest gives investors additional insight about dislocation risk if short squeezes were to occur.
  o If regulators argue that the “lifecycle” of short selling can convey a signal, they implicitly tell market participants that short sellers have better information. This may encourage herding behaviour based on historic short selling disclosures where more weight is given to the fact short selling occurred rather than attempts to independently value the asset.

The current lack in functionality is expected to change when the CAIS becomes operational. This system would allow regulators to map individual traders to their FDID’s and thus pull CAT information specifically for individual traders. Thus, while technically feasible, pulling data from CAT for specific traders is difficult, but will become much less so when the CAIS system becomes operational.
• The data collected via Proposed Form SHO is unlikely to significantly improve “oversight of financial markets and compliance with existing regulations” (p.7), or assist in “reconstructing unusual market events, including instances of extreme volatility” (p. 29).
  o By contrast, the CAT system, which is currently being enhanced, should provide the SEC with stronger analytical capabilities. For example, in relation to the specific concern of manipulative short selling, future CAT data should expedite analysis and detection.
  o Given the low frequency of situations of extreme volatility, there is concern whether the additional insight (that could be obtained through additional data, such as historical lifecycles on short sales) is significant enough to warrant its cost, which will ultimately be borne by investors.

• The costs associated with tracking and producing the daily activity data required in “Information Table 2” of Proposed Form SHO would be particularly onerous for managers.

Why well intended regulatory protection/intervention can increase risks and distress:

• In relation to improving the Commission’s “ability to respond to similar market events in the future” (p. 7), the newly proposed data framework will not provide timely insight for the SEC to act given that it is monthly data with 14 days delay after month end.
  o More importantly, it is unclear how the SEC will respond or intervene in “market events”, and how it establishes what constitutes a disorderly market and distinguishes it from a justified price correction.
  o In the context of GameStop, it should come as no surprise that a stock involved in a “social media” frenzy among retail investors and a potential short squeeze will likely experience significant volatility. But it is important to remember that markets provide a mechanism for balancing supply and demand, falling prices provide an incentive for other market participants to start buying and vice versa. The risks involved provide a deterrent for both short sellers and “long” investors to take excessive risk, and the markets certainly provide occasional lessons for those who take (excessive) risk, which is a healthy reminder to implement robust risk management practices, such as those included in the SBAI’s Alternative Investment Standards\(^8\) applicable to alternative investment managers.
  o It could be detrimental if regulators create the impression among investors that they have tools to intervene to mitigate incidents of price risk and protect investors from volatility. This would, in fact, reduce the incentive for market participants to account for and manage such risks. In fact, such false comfort might encourage investors to actually take more risk than they can afford.
  o There is further concern that potential (well-intended) regulatory interference in price formation or discovery or restrictions of market activity can exacerbate distress: The regulator signals that there are concerns in relation to market integrity, resulting in more investors withdrawing from the market, reducing liquidity at the worst possible time.

• The SBAI is not aware of any cases where short selling has had adverse effects on financial stability or caused systemic risk. In fact, recent research by the European Central Bank suggests that it is the

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\(^8\) Alternative Investment Standards: [https://www.sbai.org/standards.html](https://www.sbai.org/standards.html) (section C covers risk management (Standards 9-20))
removal of the ability to sell short (short selling bans) which has a destabilising effect. It is also worth pointing out that the episode of volatility involving GameStop and other so called ‘meme’ stocks did not constitute a systemic risk event.

- The proposing release suggests that the daily activity data (included in the “Information Table 2” of the Proposed Form SHO) “would assist the commission in assessing systemic risk” (p.29).
- The SBAI has no evidence that short selling of equity securities or volatility in markets (due to a short squeeze) give rise to systemic risk, i.e. the risk of causing the collapse of an entire financial system or market.
- The research by the European Central Bank on “Short-selling bans and bank stability”9 finds that, “contrary to the regulators’ intentions, financial institutions whose stocks were banned experienced greater increases in the probability of default and volatility than unbanned ones, and these increases were larger for more vulnerable financial institutions. Moreover, short-selling bans did not appear to support the stock prices of financial institutions whose shares were banned. (…) The results show that short-sale bans are destabilizing for the financial institutions whose shares are banned (…)”

Thank you for the opportunity to provide comments on the Proposal. If you have any questions on our comment letter, please feel free to contact Thomas Deinet at +44 203 405 9043.

Respectfully Submitted

Thomas Deinet
Executive Director – The Standards Board for Alternative Investments www.sbai.org

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